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May 9, 1997

CINERGY.

The Honorable John D. Dingell
Ranking Member
Commerce Committee Democratic Office
564 Ford House Office Building
U.S. House of Representatives
Washington, D.C. 20515

Dear Mr. Dingell:

Thank you for your April 10, 1997, letter to Cinergy's CEO Jim Rogers outlining a series of questions regarding restructuring of the electricity industry. I am pleased to provide the following responses, with the understanding that we may wish to provide additional information to you in the future.

Question 1. *From your company's point of view, is it necessary for Congress to enact legislation bearing on retail competition, and why? If you favor legislation, please outline which issues should be addressed and how you think they should be resolved.*

Cinergy strongly believes that Congress needs to enact legislation requiring states to provide for retail customer choice by a date certain to avoid a patchwork quilt of different and possibly conflicting state programs. On April 17, 1997, Mr. Rogers was able to express our views on this subject in person to members of the Energy and Power Subcommittee at a field hearing in Richmond, Virginia. The following points are provided directly from his written statement for that hearing:

"The Benefits of Competition

"Before I get into the need for federal legislation on customer choice, it is probably useful to summarize just why customer choice should be pursued in the first place. The first point is fundamental – all customers should be able to choose their electricity supplier. It's simply the right thing to do. In today's financially and technologically evolving energy markets, is there a rational and compelling reason why governments should make the decision for customers as to which supplier they may purchase electricity from and at what price? We have seen that competition in other industries brings lower prices, efficient and more innovative services, and more choices for customers – is there reason to believe that those same benefits would not come to electricity customers?

"The second point is practical – embracing competition is simply good public policy. Competition works – it drives down prices and spurs innovation. Some estimate that the benefits to the U.S. economy that will result from lower electricity prices will exceed $60 billion annually. This will occur not only through reductions in customer bills, but also through reductions in the costs of goods and services that have embedded into them the price of electricity. If the steel, aluminum, plastic, and rubber that go into auto parts are less expensive to produce, so will be the car. And just about any other product you can name. These are benefits with which everyone can identify. Simply put, a free and competitive market can and will allocate society's resources

more efficiently than governmental command and control – that is a bedrock principle of our American economic system.

"The Need for Congress to Act

"Cinergy believes that a comprehensive federal approach to retail customer choice and utility industry restructuring is not only desirable but necessary to avoid a patchwork quilt of state programs. Nearly every state in the Union is examining, at least in the broadest sense, the issue of whether and in what manner to implement customer choice in its own retail markets. Of interest to states that already have enacted customer choice, two premier questions that are likely to arise in the federal debate are those of reciprocity and "grandfathering" – will neighboring states be allowed to "play" and will the actions already taken by states be protected. Actions within Cinergy's own retail service territory are indicative of the variety of approaches to competition being taken by states that have not yet enacted new laws. In Ohio, the General Assembly has formed a bipartisan committee to study this issue and has stated its intention to release a report on customer choice legislation by the fall. Introduction and passage of a comprehensive bill is expected next year. In Indiana, with Cinergy's support, a customer choice bill was introduced this year, but the state's legislative effort has now been referred to a study committee. In Kentucky, the Commission and certain stakeholders have expressed reservations about the benefits of retail competition in an already low-cost state. Thus, discussion of customer choice legislation there is very preliminary.

"By contrast, states such as California, Massachusetts, New Hampshire, and Rhode Island are very far along in their move to retail competition. Pennsylvania, one of our neighboring states, passed legislation at the end of last year that initiates customer choice pilot programs this year and phases in full customer choice over the next several years.

"Given the undeniable economic benefits resulting from replacing command and control regulation with competition and customer choice, can anyone seriously argue that we should await action by all of the states before this policy becomes the law of the land?

"This is not an academic question. If consumers in any state are to enjoy the full benefits of competition, there will be a need for certain minimum uniform standards, or "rules of the road." Standards to govern, for example, the open access operation of local distribution wires are necessary to ensure dependable, non-discriminatory production and delivery of electricity. Only Congress can do this.

"It is neither illuminating nor even accurate for opponents of federal customer choice legislation to characterize the debate in terms of Washington infringing on the rights and powers of the states. Mr. Chairman, your legislation envisions the states exercising control over the local wires. They will have primary responsibility for universal service, the rights of local distribution customers, continuation of necessary programs for low-income customers, reliability standards, and codes of conduct. During the transition to competition, it will be the states who will determine the thorniest issue of them all – recovery of so-called "stranded costs."

"But electricity is an interstate commodity. Electrons know no state boundaries. Congress, with constitutional authority over interstate commerce, must ensure that all Americans have the opportunity to share in the benefits that competition will bring. Only a federal bill with a framework for reform can do that.

"In addition, there can be no legitimate policy-based argument for continued government regulation – whether federal or state – of aspects of the electricity business that are competitive.

"Generation is no longer a natural monopoly. It should be completely deregulated. Only Congress can do this in a comprehensive manner at the same time throughout the country.

"Further, states' rights cannot be an excuse for denying to any customer of electricity a choice of suppliers. This is not a matter of federal versus state authority. It is a question of individual rights versus government regulation; of the free market versus one controlled by regulators. Every state law that grants an exclusive franchise to a seller of electricity should be terminated on a date certain in the near future. Only Congress can do this in a manner that helps ensure fair and consistent treatment of stakeholders throughout the country.

"And finally, only Congress can remove existing federal constraints to competition, including outdated statutes like the Public Utility Holding Company Act (PUHCA) and the Public Utility Regulatory Policies Act (PURPA). While both laws may have served useful purposes in the past, they are outdated and unnecessary in competitive markets and should be repealed as soon as possible."

Question 2. *If the state(s) you serve has adopted or is considering adopting retail competition, what are your biggest concerns? Please be specific. Indicate how you are dealing with them and any recommendations you may have.*

Each of the states we serve (Indiana, Kentucky and Ohio) is considering retail competition.

In Ohio, a joint select committee of the legislature has been appointed to make recommendations as to industry restructuring by October 1, 1997, and the Governor has indicated a strong preference to adopt customer choice legislation if that is the recommendation of the joint select committee. The committee has undertaken a rather aggressive schedule of hearings at which a large variety of industry stakeholders has appeared and presented their views. Cinergy is actively participating in this process and is hopeful that legislation will be adopted during the present legislative session, which ends December 31, 1998.

In Indiana, Cinergy, together with another investor-owned utility and a coalition of industrial consumers, supported the introduction of S.B. 427, which would have afforded all customers the opportunity to choose their supplier of electricity effective October 1, 1999. The proposed legislation has been referred to a study committee for further review. The Indiana legislature has now adjourned for 1997.

In Kentucky, the Public Service Commission has been engaged in informal discussions with the various stakeholders in the restructuring debate and is considering whether or not legislation is appropriate for the Commonwealth. The legislature, which will not convene in general session again until January 1998, is going to conduct informational sessions on electric industry restructuring through its interim Energy Committee in September and October of 1997.

One challenge presented by utility operations in all three states is that the states will provide customer choice either at very different times or under inconsistent or even conflicting "rules of the road." Federal legislation that would require states to act before a date certain to allow all customers to simultaneously choose their electricity supplier would enhance the opportunity to get timely action in each of these states. Further, federal legislation could set forth a basic policy framework for customer choice (leaving implementation details to the states) so that companies such as ours, which operate in more than one state, do not face inconsistent laws and rules governing competition.

While Cinergy thinks that umbrella federal legislation requiring states to act by a date certain is necessary, we also think that each state should be permitted to fashion its own mechanisms for implementing the transition from a regulated generation market to a competitive market, as well as the recovery of stranded costs by its jurisdictional utilities.

Question 3. *Whether or not you favor federal legislation, please indicate your position on the following specific issues (to the extent not addressed in your responses):*

a. ***A Federal mandate requiring states to adopt retail competition by a date certain.*** *If retail competition is under consideration in the state(s) you serve, do you believe Congress should provide additional direction or authority?* Yes, see above response to Question 1.

b. ***Recovery of stranded investment.*** *If the state(s) you serve already has adopted retail competition, how was this issue addressed and are you satisfied with the outcome? If your state(s) is considering adopting retail competition, how would you recommend that this issue be treated? Do you think Congress should enact legislation relating to stranded cost issues, and if so what would you recommend? Is securitization a useful mechanism for dealing with stranded costs, and whom does it benefit?*

As stated above, Cinergy is actively promoting customer choice legislation in the three states we serve - Ohio, Indiana, and Kentucky. Stranded cost recovery is a key issue in each state, although no state has yet fashioned a solution. Without belittling the significance of any party's equity concerns, we believe the best public policy with regard to the recovery of stranded costs is to focus on practicality, by which we mean finding the quickest resolution to the issue that is reasonably efficient and sufficiently acceptable to all parties so that transition to retail access can proceed expeditiously. If, as we believe, such acceptance can be obtained most expeditiously by providing in some manner for stranded cost recovery, then recovery should be viewed as in the public interest. Simply stated, we do not want to see litigation over stranded cost recovery derail the movement toward customer choice. Because what constitutes an acceptable resolution to stranded cost issues may vary from state to state, Congress should not restrict the states in their approaches to addressing this issue.

It is for this reason that Cinergy, in the three states in which it operates, supports a price cap approach to the recovery of stranded costs that places squarely on the utility the responsibility for managing its stranded costs over a defined period of time while giving to consumers price stability during the transition period. Properly structured, the price cap gives the utility the maximum incentive to make its costs more competitive during the transition because the utility takes the risk at the end of the transition if its costs are not competitive. The price cap also reduces the risk that litigation will derail or substantially delay competition by avoiding the need to quantify a mythical "stranded cost number." Quantifying stranded cost recovery amounts in advance is difficult and risky, largely although not exclusively because actual market prices will turn out to be different from whatever forecast of prices is used for the initial stranded cost estimate. If market prices turn out to be higher than the forecast, the recovery amount that customers pay utilities will be more than the actual stranded costs; vice versa if prices turn out lower than the forecast. Further, the possible financial consequences of forecast error for both sides are large enough that the process of reaching agreement on fixed stranded cost recovery is likely to be both contentious and time-consuming. In our view, it makes more sense to adopt a recovery approach which frees both sides from having to make a major bet on future market prices.

Securitization of stranded costs has the potential to reduce utility financing costs and thereby reduce either the prices paid by customers, the transition cost exposure faced by utility shareholders, or both and may, therefore, serve as a tool to facilitate a transition to retail access.

c. ***Reciprocity.*** *Can states condition access to their retail markets on the adoption of retail competition by other states? Should Congress enact such a requirement? Could such a requirement create an incentive for states with low electric rates not to adopt retail competition, in order to keep cheap power at home?*

The demand for reciprocity will arise primarily in the situation where one state has adopted retail competition, and suppliers located in a state that has not yet adopted retail competition attempt to serve retail customers in the state with competition while not affording their own customers a choice. Federal legislation mandating customer choice in all areas of the country at roughly the same time can go a long way toward eliminating or mitigating this aspect of this issue.

Question 4. *If Congress enacts comprehensive restructuring legislation, should it mandate "unbundling" of local distribution company services? What impact would this have, and would the effects differ for various customer classes? Would this entail substantial expense, and who would incur any such costs?*

Unbundling of the rates and charges of the various components of previously bundled utility service will be necessary for retail competition to proceed. We do not believe that such unbundling will entail prohibitive expense, and such unbundling should not necessarily impact any customer class. States should be given latitude on how they deal with the issue of inter-class subsidies. Approval of unbundled tariffs is the sort of implementation detail that the states can manage and should not need to be addressed in federal legislation.

A competitive market requires that a distribution company provide distribution services on a comparable basis to all electricity suppliers, without discrimination. Accordingly, it is essential that comprehensive restructuring legislation require each covered distribution company to have on file and in effect with the state utility regulatory commission a distribution comparability tariff. The comparability tariff would set forth the rates, charges, terms, and conditions under which the distribution company offers to provide distribution services for power supplied by a third-party supplier for delivery to the ultimate customer of the third-party supplier. Those rates, charges, terms, and conditions must be comparable to those offered by the distribution company to provide such services to itself or an affiliate of the distribution company to provide power to its ultimate customer. The rates, charges, terms, and conditions of such tariff should only reflect the rendering of distribution services. That is, any generating or transmission-based rates, charges, terms or conditions should be unbundled from those set forth in the distribution comparability tariff.

While a competitive market requires the functional unbundling of the generating function, the transmission function, and the distribution function, it does not require the further unbundling of the various distribution services. So long as adequate codes of conduct or affiliate rules are in place, distribution services may continue to be provided without adverse impact on competition without further unbundling. The determination of such codes of conduct or affiliate rules should be left to the states so that they can be tailored to fit their unique circumstances and economics.

Question 5. *Recently Chair Moler of the Federal Energy Regulatory Commission recommended that, as part of comprehensive legislation, Congress authorize the Commission to enforce compliance with North American Electric Reliability Council standards to help maintain reliability of service. Do you believe this is necessary, and why or why not?*

With respect to transmission and system operations, the Federal Energy Regulatory Commission should be given authority to enforce reliability standards for the electric utility industry. This authority should be considered by Congress, even in the absence of legislation on retail

competition, to ensure that wholesale markets develop in a workably competitive manner consistent with sound reliability principles.

Once authority to enforce reliability standards is given to FERC, the Commission could defer to NERC the development of proposed standards. However, FERC must review NERC's process for the development of reliability standards to ensure that it is a fair and open process. In addition, before the proposed standards are adopted by FERC, they should be subjected to the appropriate regulatory approval process.

In all instances FERC should incorporate the reliability standards into the Code of Federal Regulations and be responsible for their enforcement.

Distribution reliability is more appropriately addressed at the state level, while generation reliability should be managed through contractual and market mechanisms.

Question 6. *What concerns does your company have with respect to the role of public power and federal power marketing agencies in an increasing competitive wholesale electric market? In markets in which retail competition has been adopted? Are there concerns you would like to have addressed if Congress enacts comprehensive restructuring legislation? Should Congress consider changes to federal law as it applies to regulation of public or federal power's transmission obligations?*

Cinergy's direct wholesale market experience with certain publicly funded entities suggests that for their participation in the bulk power markets to be fair they, like the privately owned utilities, must functionally separate their transmission and generation businesses. A failure to functionally separate the transmission and commodity businesses leads to potential competitive abuses and difficulties in securing transmission service from such entities on fair and comparable terms. Transmission service must be available from these entities on the same basis as from other owners without having to resort to administrative intervention by the FERC to secure such service.

In the future, Congress will have to consider how to reconcile the continuation of tax and other advantages for one class of power sellers that are not available to others. In the long run, such entities should be allowed to compete for retail customers outside their traditional areas only if their own ultimate retail customers have a choice of suppliers.

Question 7. *If Congress enacts comprehensive restructuring legislation, should changes be made to federal, state or local tax codes, and if so, why? Please be specific.*

The electric utility industry has historically been a major source of state and local tax revenue for reasons of both efficiency and effectiveness. Because demand for electricity is relatively inelastic, taxes on electric utilities have probably distorted economic efficiency less than would have been the case with taxes on other products and services for which good substitutes were more readily available. Further, as regulated monopolies, utilities have been effective tax collectors: taxes levied on utilities could be passed on to customers through electric rates and customers, the ultimate taxpayers, could not easily bypass them. Although in recent years, exceptions have arisen – notably in the case of large consumers who can bypass electricity taxes by purchasing ge fuel and generating their own electricity – for the most part taxes on electric utilities have remained a reliable and reasonably efficient source of revenue for state and local governments.

Unfortunately, many state and local electricity taxes are structured in ways that did not contemplate competition in electricity. Specifically, because the majority of utility assets and revenues relate to generation services, utility property taxes and gross receipts taxes work as well

as they do only because of utilities' status as monopoly sellers of generation. When consumers gain the ability to purchase equivalent but untaxed generation services from non-utility and out-of-state utility suppliers, utility generation-based taxes will be both ineffective and inefficient. The ineffectiveness is obvious: a tax that can be avoided simply by purchasing from non-utility A or out-of-state utility B rather than local utility C is likely to be bypassed frequently, leading to lower tax receipts. The inefficiency arises in cases where non-utility A or out-of-state utility B actually has higher production costs than local utility C but wins the sale anyway because utility C is subject to the utility tax. Such instances would lead to misallocation of resources and could reduce or eliminate the economic benefits of competition. The possible solutions to this problem are either to broaden the application of electricity taxes so that all potential generation suppliers in the competitive market are equally taxed, or else to restructure electricity taxes into a form that can be assessed and collected on distribution service where utilities will retain local franchise monopolies.

Although the more significant tax issues related to industry restructuring will occur at the state and local level, federal tax reform would also be beneficial in certain areas. First, as at the state level, the existing federal tax structure would distort competition in a restructured electricity industry. Municipal utilities, rural electric co-ops and federally owned utilities, none of which pays federal income tax and many of which receive other taxpayer-provided subsidies, currently account for approximately 24 percent of retail electricity sales in the United States. To the extent that these entities are permitted to expand their operations following deregulation and their success in doing so is a result of tax advantages and subsidies, the efficiency benefits of competition will be reduced; the federal government could also experience a tax revenue loss as a consequence. A second federal tax problem relates to the incentives for individual utilities to restructure. Industry restructuring could lead to significant utility asset sales as the present vertically integrated utilities, either voluntarily or under protest, divest themselves of certain assets or functions. Under current law, such transactions would most likely have a significant federal income tax cost, reducing their attractiveness. A tax law change mitigating this result would be desirable to encourage more voluntary restructuring where such activities appear consistent with the pro-competition policies guiding the industry restructuring initiative.

Question 8. *What, if any, concerns do you have about the reliability of the electric system? If the industry moved to retail competition, will adequate reserves be available? Is the transmission system capable of handling full retail competition?*

The reliability of the electric system can be maintained and perhaps even improved with competition. The increased number and complexity of transactions can be successfully managed because of industry structural changes, reliability council initiatives, technical innovations, and the formation of independent system operators (ISOs).

FERC Orders 888 and 889 have required the separate operation of utility marketing and reliability functions which increases the focus on reliability in utility control centers. Utility reliability groups have developed processes and procedures to maintain reliability in a competitive environment. These include methodologies to calculate available transmission capacity, procedures to track transactions from the generator to the load, the establishment of regional security coordinators, and mandatory compliance with reliability standards.

Technology will also play a role. Newer, smaller, more efficient gas generating units can be installed in a short period of time to address transmission constraints. Also, new transmission technology will provide increased capacity on existing lines.

The establishment of ISOs will be the most significant factor in the maintenance of reliability. ISOs will have the information, responsibility, and authority necessary to preserve reliability.

In a fully competitive retail environment, the level of generation reserves will generally be dictated by the needs of the customer. Customers with firm requirements will contract for desired reserves and other customers will buy only when generation resources are available.

The transmission system is highly interconnected and today is moving large quantities of power in the wholesale market. Even though some transmission congestion can be expected, the system can handle full retail competition. Additional transmission facilities will be built if they can be supported by the economics of the market, or generators will locate near the load centers if that is a more economic alternative.

Question 9. *If Congress enacts legislation on retail competition, should changes to the Public Utility Company Holding Act of 1935 (PUHCA) be included? If so, what would you recommend? In particular how should Congress address market power concerns in any such legislation? Are transition rules needed during the period before effective competition becomes a reality?*

Before the issue of retail electric competition arose, over 15 years ago the SEC supported outright repeal of PUHCA as an outdated and redundant statute; on this basis alone, the case can be made for repeal of PUHCA.

However, there is now a more urgent reason for repeal; namely on-going developments in the utility business, including increased retail and wholesale competition fostered by the Energy Policy Act (EPACT), FERC and state initiatives, the convergence of electric and gas utility businesses, the growth of national energy service companies and power brokers and marketers and advances in electric and information technologies; PUHCA, with its (a) strict geographic limitations, (b) broad definitional scope to include all electric transmission and distribution facilities and, after EPACT, retail generation facilities, and (c) pervasive regulatory and corporate structure requirements impedes, if not prohibits, the entrants of competitors into these new, and developing, energy markets and businesses; PUHCA was designed in 1935 to provide a structure for the then electric and gas industry; that structure is inconsistent with, and because of its rigidity is ill-adapted to respond to, the on-going changes today in the utility and energy businesses; in our answer to Question 11 we provide examples of these PUHCA issues.

The reasons for PUHCA repeal are, consequently, in our view, much larger than retail competition. Nevertheless, PUHCA repeal is mandatory in order for the states truly to offer retail competition to their residents. Absent repeal, the states are not able to maximize the universe of potential competitors and thus deprive residents of true competition. Solely because of their corporate structure, holding companies (registered and exempt alike) are constrained geographically by the terms of PUHCA and thus cannot own or operate various utility facilities in distant states. Thus, all states seeking retail competition are deprived of a large number of potential players.

Cinergy continues to support the repeal of PUHCA in a manner generally consistent with the SEC's June 1995 recommendation, either as part of comprehensive reform of the electric industry or as separate legislation.

It is unnecessary for Congress to address market power concerns in PUHCA repeal legislation. PUHCA was created to address primarily investor abuses; other governmental authorities (the FERC, the Department of Justice and the state PUCs) are in place, and have the power, to address market power concerns that may arise. As an example, FERC's newly announced merger policy statement focuses specifically on market power concerns.

Transition rules are not necessary in connection with the repeal of a statute, like PUHCA, which has become outmoded and affects, through its prohibitions, the movement to competition in various energy and energy related markets.

Question 10. *To what degree, if any, have recent Securities and Exchange Commission administrative orders and Rule 58 decreased the need for legislative changes to PUHCA? Assuming these actions withstand any court challenges, what are your major remaining concerns about the Act?*

We support the SEC's recent administrative orders and Rule 58 and the effort of the SEC, in part, to reduce unwarranted federal regulatory burdens; unfortunately, as the SEC itself recognized in its 1995 report, the SEC does not have the authority, on its own, to remove PUHCA's more significant constraints and burdens which restrict the development of competitive utility and energy markets; only repeal can accomplish this result; even if the SEC had greater exemptive authority, given the regulatory process, the SEC would not be in a position adequately and timely to respond to the changes in the utility and energy businesses, due to the diversity and frequency of such changes.

We have the following other major concerns with PUHCA:

(1) Geographic limitations on ownership of utility businesses and properties in a changing, and increasingly competitive, utility business.

(2) Limitations on combinations of electric and gas companies in a changing national energy environment.

(3) Limitations, regardless of size, on foreign and domestic non-utility investments.

(4) Given the need for rapid response to competitive changes, unnecessary delays in the receipt of SEC regulatory approval for various routine business transactions including, among others, financings, extensions of credit, immaterial investments in utility and non-utility businesses, various declarations of dividends and proxy solicitations.

(5) The on-going cost of compliance with an extremely comprehensive (but, in many respects, redundant) regulatory statute at a time in which all utilities must reduce costs.

We believe that these concerns have adverse impacts on consumers since they either limit competition in utility, energy-related and non-utility markets or increase, unnecessarily, the cost of doing business.

Question 11. *As electricity markets have become more competitive, some have asserted that PUHCA prevents consumers from receiving the full benefit of competition. Do you agree or disagree, and why? Is competition in wholesale or retail electric markets dependent upon the participation of the registered holding companies? Is it a certainty that changes to PUHCA would enhance actual competition? Please provide specific examples to illustrate your answers.*

As mentioned in our responses to Questions 9 and 10, we firmly believe PUHCA prevents consumers from receiving the full benefits of competition. This results from the structural and geographic limitations in PUHCA which either prevent, or inhibit, competitive entrance into various emerging electric utility and energy services markets. There are a number of examples in this regard:

(1) PUHCA's geographic limitations on ownership of retail generation assets by utilities and PUHCA's requirement of a single integrated utility system for registered holding company systems -

These limitations and requirements prevent, in significant part, Cinergy and other utility systems from owning retail generating facilities in geographic areas other than their current utility service areas; as a result, for example, PUHCA restricts full participation in bidding on ownership of generating facilities which may serve retail loads as part of disaggregation initiatives in various U.S. locations, including those underway in New England and California; this could reduce the number of bidders and, consequently, also potentially the price received.

(2) Geographic limitations on ownership of electric distribution and transmission facilities -

PUHCA restricts or prevents investments by Cinergy and other utilities in discrete transmission or distribution facilities or substations for the purpose of competing with the local utility to provide services to retail loads; again PUHCA reduces the number of entrants into new competitive markets.

(3) Limitations on ownership of utility facilities by non-utility companies -

PUHCA has limited exemptions for ownership of utility facilities by non-utility companies; as a result, the pool of potential entrants into emerging utility markets is further limited.

(4) Limitations on "operation" of utility facilities, including transmission, distribution and retail generation -

PUHCA's geographic limitations cover "operation" as well as "ownership" of dispersed electric transmission, distribution and retail generation facilities; consequently, PUHCA restricts the number of potential competitors to operate transmission systems under ISO programs or to operate power plants or other utility facilities as part of the newly emerging energy services business.

The participation of registered holding companies in wholesale or retail electric markets necessarily enhances competition by increasing, significantly, the pool of potential participants with expertise in these developing markets.

Given the scope and number of markets for utility and/or energy services to which PUHCA limits access, as noted above in this Question 11, we believe that actual competition will increase if PUHCA is repealed; this was certainly the case in one market, the wholesale generating market, with the adoption of PURPA and EPACT and their PUHCA exemptions.

In addition, PUHCA's repeal would increase competition and benefit customers in other markets through the elimination of restrictions on entry by registered holding companies into non-utility businesses.

Question 12. *Do registered holding companies face unique problems if some states they serve adopt retail competition and some do not?*

The registered holding companies plan their utility resources and operations on a centralized multi-state basis, including allocation of utility resources and exchanges of power in the case of electric systems, to achieve overall efficiencies and economies for their respective systems. In addition, unlike other utility companies, they often have service companies which operate "at cost" under PUHCA, without profit or loss, and provide a broad array of services on an allocated basis to their multi-state utility affiliates. These operations, structures and cost allocations are designed to balance the interests of all consumers and investors in the registered system. Retail competition in some, but not all of the states, served by a registered system could significantly alter these unique balances by shifting costs to the detriment of certain consumers and/or the system as a whole. We think that federal legislation is necessary to limit the potential cost shifting as a result of the unique multi-state integrated operations and structures of registered holding companies.

Question 13. *How do the various retail competition proposals presently pending before the Congress affect decisions regarding stranded costs for registered holding companies? Do you support any of the formulations in these bills? Do you have alternate recommendations on this or other issues unique to registered holding companies if Congress enacts retail competition legislation?*

Our position with regard to the recovery of stranded costs is set forth in our response to Question 3b.

Given the unique operations of registered holding companies, as explained in our response to Question 12, any legislation adopted should limit the potential for cost-shifting to the detriment of certain consumers in a registered system and/or the system as a whole.

I hope that these responses are useful in your ongoing review of electric industry restructuring. Should you need additional information or clarification of any of the above information, please feel free to contact Ms. Julie Blankenship, Manager of Federal Affairs in Cinergy's Washington office, at (202) 824-0401. We look forward to working with you on this important issue.

Sincerely,

John L. Stowell
General Manager
Government and Regulatory Affairs